



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY  
REGION III  
1650 Arch Street  
Philadelphia, Pennsylvania 19103-2029

AUG 29 2018

Mr. Scott Mandirola, Deputy Cabinet Secretary  
West Virginia Department of Environmental Protection  
601 57<sup>th</sup> Street  
Charleston, West Virginia 25304

RE: FY 2017 CWSRF Program Evaluation Report

Dear Mr. Mandirola:

This Program Evaluation Report (PER) is the U.S. Environmental Protection Agency's (EPA's) evaluation of the West Virginia Department of Environmental Protection's (WVDEP's) Clean Water State Revolving Fund (CWSRF) program. The PER summarizes EPA's evaluation and identifies strengths, discusses new indicators, and opportunities for improvement in the CWSRF program. The review covered the period July 1, 2016 through June 30, 2017. EPA conducted its on-site review from May 22 to 23, 2018.

The WVDEP is commended for timely use of available CWSRF funding. There are no unliquidated grant balances and the program's Pace is equal to the national average. As a result of EPA's review, this PER includes the following recommendations for WVDEP to consider:

1. Although WVDEP continues to make progress towards meeting the additional subsidy requirements, WVDEP has not yet executed loans for the additional subsidy it plans to provide from the 2016 and 2017 capitalization grants. In accordance with EPA's 2013 memorandum, the CWSRF annual report needs to include explanations for any delayed projects that are expected to receive additional subsidy from the 2016 and 2017 grants.
2. WVDEP executed loans to meet is Green Project Reserve (GPR) goals through SFY2017. However, during our review we noted several instances in the CWSRF Benefits Reporting (CBR) database where WVDEP was not recognizing full credit for its GPR activity. WVDEP committed to make needed corrections to CBR.

### **Purpose and Scope**

Section 606(e) of the Clean Water Act (CWA) requires EPA to conduct an annual oversight review of each State's CWSRF program. The FY 2017 annual review of West Virginia's CWSRF program was conducted in accordance with EPA's Annual Review Guidance dated December 2015 and Region III's Annual Review Plan. The annual review process includes EPA's consideration of West Virginia's Annual Report, evaluation of the State's program, coverage of items in the Annual Review Checklist, completion of the Project File Review Checklists, and issuance of this PER.

The purpose of the annual review is to assess West Virginia's management and



implementation of the CWSRF program, including:

- Performance in achieving goals and objectives identified in the Intended Use Plans (IUPs) and the Annual Report;
- Compliance with regulations in 40 CFR Part 35; EPA/ WVDEP operating agreement, and any open CWSRF grant agreements (CS-540001-14, -15, -16, -17);
- Financial status and performance of the Fund; and
- Resolution of any audit findings and prior year PER recommendations.

### **Environmental Benefits**

West Virginia's CWSRF program provides financial assistance to improve and maintain water quality throughout the State. The projects financed are vital in protecting and improving water quality in rivers, lakes, and streams throughout the State used for drinking water, recreation, cold-water fisheries, warm water fisheries, wildlife use, industrial use, and agricultural use. In addition to addressing wastewater issues, the CWSRF provides funding to projects to reduce stormwater impacts. West Virginia's CWSRF program contributes to the joint State/EPA mission of achieving clean and safe water with the following specific goals:

- Eliminate sewage overflows from combined sewer overflows (CSOs) and from separate sanitary system overflows (SSOs);
- Improve and protect designated uses of water bodies; and
- Achieve and maintain Clean Water Act (CWA) compliance.

During FY 2017, WVDEP financed 29 projects totaling approximately \$66.8 million all of which helped systems achieve compliance with standards and assisted communities with improving impaired water bodies.

### **Short and Long Term Goals and Program Accomplishments**

On pages four through six of the annual report, the State summarized its accomplishments and on-going efforts towards achieving its program goals. The Region reviewed this summary to confirm that the State continues to effectively work towards the achievement of the goals of the CWSRF program. In particular, EPA commends WVDEP for its efforts in developing effective wastewater management in rural, low income communities in West Virginia. Being able to provide principle forgiveness to fund decentralized systems allowed WVDEP to provide reliable sewer service to communities that would not otherwise be able to afford it.

### **Program Management and Staffing**

As of June 30, 2017, there was approximately \$730 million in CWSRF assets making it essential that the program remain fully staffed with adequately trained managers and personnel for WVDEP to effectively operate the CWSRF program. We recognize that WVDEP continues to effectively manage its CWSRF program. Representatives of the CWSRF program regularly attend the national Council of Infrastructure Financing Authorities (CIFA) conference, Regional All-States Meetings, Need Survey trainings and other CWSRF related training. These training opportunities are vital to WVDEP staying informed of the numerous changes and continuing developments in the national program. WVDEP continues to actively participate in all training opportunities including the recent Regional SRF 101 training session and SRF Financial training session held in Philadelphia in 2018. In addition, WVDEP managers are often requested to present at national



conferences and webinars so that their expertise may be shared with other States across the country.

Further, we appreciate WVDEP's efforts in organizing and hosting the 2017 Regional All-States Meeting in Shepherdstown, WV on April 24-25, 2018. The meeting was a huge success allowing for open and involved discussions from all participants. Representatives from all Region 3 States attended and the agenda included many topics of benefit to all.

### **Project Files Reviewed**

EPA reviewed WVDEP's files for the following two projects:

- City of Morgantown; loan closed on 12/01/2016 for \$25,500,000.
- New Haven Public Service District; loan closed on 12/06/2016 for \$1,947,707.

The project files contained adequate and complete documentation. WVDEP conducts a full technical review and ensures the state environmental review process is completed. WVDEP performs a detailed financial capability review on all new loans and includes this documentation in the file. In addition, a WVDEP engineer or project manager periodically performs site visits during the construction phase of all projects. The project files include all inspection reports. WVDEP demonstrates continued overall sound management in its projects.

### **Compliance Requirements**

EPA reviewed various documents provided by WVDEP to ensure compliance with all of the following requirements:

- Additional Subsidization\*
- Administrative Costs
- American Iron and Steel
- Annual Report
- Architecture and Engineering Contract Procurement
- Binding Commitments
- Clean Water National Information Management System (CWNIMS)
- Cost and Effectiveness
- CWSRF Benefits Reporting (CBR)
- Davis Bacon
- Federal Financial Accountability and Transparency Act
- Federal Financial Reports
- Fiscal Sustainability Plans
- Green Project Reserve\*
- Operating Agreement
- Payment Schedules
- Readiness-to-Proceed
- Signage
- State Match
- SRF Sustainability Policy\*
- Sub-award Policy\*
- Timely and Expeditious Use of Funds\*

\*Additional detail provided below

### **Additional Subsidization**

Beginning in FFY 2010, Congress authorized CWSRF State programs to provide additional subsidization. In West Virginia, this is provided in the form of principal forgiveness. Each year's capitalization grant identifies the minimum amount required by Congress to be provided as principle forgiveness. WVDEP's annual Intended Use Plan (IUP) identifies the amount of additional subsidy it plans to provide each year. Shown in the below chart is the State's progress towards committing the additional subsidy in executed loans for each capitalization grant.

<b>Grant</b>	<b>Minimum</b>	<b>Planned in IUP</b>	<b>Executed Loans</b>
2010	\$4,756,940	\$15,856,466	\$15,856,466
2011	2,133,076	7,110,255	7,110,255
2012	1,224,403	1,836,605	1,836,605
2013	980,381	1,470,572	1,470,572
2014	1,189,352	1,784,029	1,784,029
2015*	0	6,523,500	6,370,524
2016	2,082,900	8,331,600	0.00
2017	2,066,800	\$6,200,400	0.00
* Congress did not require a minimum amount in 2015. Source: WVDEP tracking worksheets.			

Since 2010, WVDEP's plans for additional subsidization exceeded the minimum amount required. For 2010 through 2014, WVDEP executed loans for the full amount of additional subsidy it planned for in its IUPs. During FY2017, WVDEP provided approximately \$4.9 million of principle forgiveness in executed loans to disadvantaged communities across the State. All of this went towards meeting WVDEP's planned amounts for the 2013, 2014, and 2015 grants. However, as of the end of FY2017, WVDEP did not yet execute loans for additional subsidy it planned to provide from the 2015, 2016 and 2017 grants.

WVDEP provides additional subsidy only to disadvantaged communities as determined by the affordability criteria outlined in the IUP. Readiness-to-proceed to construction is the primary criteria for allocating additional subsidy. The final amount of additional subsidy to be provided to a community is not determined until after construction bids are received. These procedures ensure WVDEP provides additional subsidy only where and when needed to protect the perpetuity of the Fund. However, the procedures usually result in delays in getting the additional subsidy into executed loans.

WVDEP continues to make progress towards meeting the minimum additional subsidy requirements as well as the amounts it plans that are in excess of the minimum amount. Since the end of FY2017, WVDEP provided \$4.1 million of additional subsidy in executed loans which is not reflected in the chart above. This completed the planned amount for the 2015 and the minimum required amount for the 2016 grant. In addition, WVDEP issued binding commitments for another \$3 million. WVDEP identified another 19 projects on its project priority list that are eligible to receive approximately \$21.4 million in principle forgiveness from the 2016, 2017, and future grants.



According to the memorandum from EPA issued on August 19, 2013 entitled “Questions and Answers on the Additional Subsidization and Green Project Reserve Provisions”, States must report all projects that received additional subsidy in their annual report. If the minimum subsidy funds required are not in executed loans at the end of the second year, the annual report for that year must contain a complete explanation for the reasons for the delay and provide a plan that identifies the project(s) that will use the remaining subsidy funds, along with milestones for each project showing the path to an executed loan. The Intended Use Plan for the following year is to indicate the amount of additional subsidy from the previous year(s) that still must be provided to projects. WVDEP’s IUPs always reflect its overall plan for the additional subsidy available that year. However, the annual report needs to include explanations for any delays in providing the additional subsidy to projects from prior IUPs. For the SFY 2018 annual report due September 30, 2018, WVDEP should include information on any projects delayed that are expected to receive additional subsidy from the 2016 and 2017 grants. WVDEP provided an assurance that full compliance with this requirement will be achieved.

### **Green Project Reserve**

Beginning in FFY 2010, Congress identified goals for the CWSRF State programs to commit a certain amount of funds to projects qualifying as green project reserve (GPR). These projects may be green infrastructure, water conservation, energy efficiency, or environmentally innovative. Each year’s capitalization grant identified a specific minimum amount to meet the goal. The CWSRF Policy dated December 22, 2011 explains that States are required to identify projects in their Intended Use Plan (IUP) at least equivalent to the GPR amount or meet the requirements for a waiver. WVDEP consistently identifies an adequate amount of GPR projects in its annual IUPs to meet this minimum goal amount; therefore, WVDEP complied with the requirement.

EPA’s Questions and Answers memorandum on the GPR Provisions, dated August 19, 2013 states that GPR projects should be in executed loans within two years or the state must provide information in the following annual report on how they intend to move the GPR projects from the IUP to executed loans. The below chart summarizes the State’s status in executing loans for the GPR projects identified on its IUPs.

<b>Grant</b>	<b>Minimum</b>	<b>Executed Loans</b>	<b>Compliance</b>
2010	\$6,352,400	\$6,352,400	Achieved
2011	4,603,800	4,603,800	Achieved
2012	2,203,100	2,203,100	Achieved
2013	2,081,300	2,081,300	Achieved
2014	2,185,600	2,185,600	Achieved
2015	2,174,500	2,174,500	Achieved
2016	2,082,900	2,082,900	Achieved
2017	2,066,800	3,628,492	Achieved

During the review, it was noted that WVDEP was not recognizing in CBR, all GPR activity. WVDEP committed to make needed corrections to the CBR database and EPA agreed to work with them as needed.

WVDEP executed loans to meet its GPR goals for all grants from FY2010 through FY2017. In addition, WVDEP exceeded its FY2017 goal by over \$1.5 million. WVDEP’s success is based



on its commitment to accept applications in all four GPR categories, its willingness to consider innovative projects, and its policy of offering principle forgiveness to communities for a portion of project costs that meet the GPR criteria. We commend WVDEP for its success in achieving this goal.

### **Sustainability and Resiliency**

During the annual review of SFY2014, EPA held a detailed discussion with WVDEP managers following the 14-page “SRF Sustainability Conversation Guide” dated August 13, 2014. Topics included asset management, planning, alternative analysis, rate structures, green infrastructure, decentralized wastewater systems, green space, energy efficiency, energy audits, renewable energy, water efficiency, water audits, water reuse, consolidations and partnerships, resiliency, security, emergencies, and recovering from extreme weather events.

During this year’s annual review, EPA and WVDEP furthered this discussion by focusing on some specific CWSRF program initiatives, projects recently funded, and projects planned to be funded. The discussion was focused on the Sustainability tab from EPA’s SRF Annual Review Checklist. In summary:

- Decentralized systems, for individual homes or small communities, are categorized as environmentally innovative under the green project reserve (GPR). WVDEP established partnerships with two organizations to assist in providing low-interest loans to repair, replace, or install new (when only a direct pipe exists) septic systems. During FY 2017, 41 individual homeowner septic systems totaling over \$2.8 million were built.
- Also in FY2017, the small community of Winona, WV in the New Haven Public Service District received a \$5.17 million loan, including \$2.43 million in principle forgiveness. The new decentralized system utilizes green technology that includes a septic tank effluent pump (STEP)/septic tank effluent gravity (STEG) system. The project replaces failing septic systems and straight pipes for 99 homes that caused untreated and partially treated wastewater to contaminate several nearby streams. The principle forgiveness and efficient technology made this project a long-term sustainable solution for this community by ensuring low operation and maintenance costs in a community with user rates at 2.24% of median household income.
- WVDEP offers principle forgiveness incentives for projects that qualify under the green project reserve, independent of the affordability criteria. An applicant may receive principle forgiveness equal to the lower of \$500,000 or 50% of the portion of their project that qualifies as either: green infrastructure, water conservation, energy efficiency, or environmentally innovative. WVDEP raised the percentage from 25% to 50% during FY2017.

In FY2017, with this incentive, the City of Morgantown received a \$25 million CWSRF loan that included \$2.9 million of energy efficient improvements. The City received the maximum \$500,000 in principle forgiveness. Morgantown’s project implements its Long-Term Control Plan for combined sewer overflows.

### **Subaward Policy**

EPA discussed with WVDEP the Agency’s new Sub-Award Policy and its applicability to the CWSRF Program. In summary, the policy applies to the CWSRF, if WVDEP awards any of its additional subsidy in the form of grants. The Policy outlines the State’s responsibilities in

implementing the new uniform grant guidance (UGG) at 2 CFR 200 330-332 in its oversight of any subawards, i.e. CWSRF subgrants. WVDEP confirmed that their additional subsidy is provided in the form of principle forgiveness. WVDEP reviewed the Subaward Policy and understands its responsibilities for overseeing these subgrants, if WVDEP ever changes its policy.

### **Cash Transactions Reviewed**

EPA Region 3 selected a sample of four transactions listed below, totaling \$4,069,994. EPA staff reviewed the supporting documentation for the selected cash draws. All invoices reviewed were found to be properly made for eligible CWSRF expenditures and were appropriately recorded in WVDEP's accounting records. No costs were questioned and there were no improper payments.

Cash Transactions		
Grant #	Date	Amount
CS-540001-16	8/02/2016	\$916,649.00
CS-540001-16	8/23/2016	\$1,047,125.00
CS-540001-16	10/14/2016	\$1,507,929.00
CS-540001-16	11/18/2016	\$598,291.00
Total		\$4,069,994.00

In addition, EPA Regional staff reviewed the list of negative draws provided by EPA Headquarters. There were no negative draws for West Virginia's CWSRF grants.

### **Unliquidated Obligations (ULOs)**

Nationally, EPA is concerned with the amount of undrawn grant funds because funded projects are intended to be shovel ready and funds expended timely. Failure to do so creates an appearance that the funds are not needed, increases the potential for rescission of unexpended funds, and may lead to possible reductions of appropriations in subsequent years. West Virginia continues to follow EPA's first-in-first-out policy of drawing grant funds such that older grant funds are drawn first. In addition, EPA's guidance encourages States to have no more than two open capitalization grants at any one time. West Virginia met this goal as well. As of our review in May 2018, WVDEP drew 100% of all capitalization grants through the FFY 2017 grant, resulting in a ULO balance of \$0.00.

### **Program Pace and Timely and Expeditious Use of Funds**

The Loans to Funds Available (pace) indicator represents the percent of money available in the CWSRF program which is committed in executed loans. In FY 2017, WVDEP achieved a pace of 98%. This percentage is equal to the national average for the CWSRF program. WVDEP identified a pipeline of projects to fund in the future which will ensure continued success in meeting the fund utilization goal rate. EPA commends WVDEP for its expeditious and timely use of all available funds.



## **Septic System Loans**

Septic repair and replacement projects are administered by the West Virginia Housing Development Fund (HDF) and Safe Housing and Economic Development (SHED), Inc in partnership with the WVDEP's CWSRF program. HDF and SHED act as fiscal intermediaries with the homeowners. All septic loans are high risk because the borrowers are generally low income with inadequate collateral so they are unable to borrow from a commercial bank. WVDEP's partnerships with HDF and SHED provide very low interest rate loans to these homeowners to ensure they have access to sanitary septic systems that protect human health and the environment.

Given the riskiness of these loans, the CWSRF program developed several detailed procedures to ensure diligent efforts by HDF and SHED to collect the outstanding balances of the septic loans. These procedures include specific steps to timely address any delinquent accounts. A delinquent account is one where the borrower has missed one or more monthly payments on their outstanding loans. As of June 30, 2017, HDF and SHED had initiated collection procedures on 130 delinquent accounts totaling \$130,109.

During FY2017, four recipients declared bankruptcy and their outstanding loan balance became uncollectable, totaling \$14,453. In addition, three other recipients totaling \$7,650 were delinquent for more than a year. To resolve these seven uncollectable accounts, WVDEP transferred \$22,103 from its administrative fee account into the Fund. This transfer replenishes the Fund so there was no net loss to the CWSRF from these loans.

Although septic loan delinquencies and uncollectable accounts represent less than 0.3% of the CWSRF Fund balance, WVDEP continues to closely monitor this high-risk portion of its CWSRF's loan portfolio. Should data trends indicate significant increases in delinquencies or uncollectable accounts, WVDEP will determine if any procedural changes are needed.

## **Financial Health of the Fund**

The overall financial health of the CWSRF program is good. All municipal loans are secured by revenues from user charge systems and debt service reserves. Due to the absence of long-term debt, all funds deposited into the CWSRF are available to provide additional financial assistance to improve the State's water quality. To date there are no municipal loan defaults, although some municipalities are delinquent with respect to deposits of loan reserves totaling \$301,115. That is an increase over FY 2016 where delinquencies totaled \$256,999. The West Virginia Water Development Authority actively monitors the delinquent communities monthly and when necessary, files a complaint with the Public Service Commission of West Virginia for resolution of the deficiencies. Most of the deficiencies occurred in 2017. One utility, which was responsible for 72% of the total, recently increased user rates to resolve the delinquency.

As of June 30, 2017, net assets were \$728,514,744. That is 3.27% increase over FY 2016 net assets of \$705,441,591. Included in this amount is \$421,428,934 in loan principal and interest repayments and \$29,454,718 in investment earnings.

Return on Equity (ROE) is a measure of the growth of capital within the CWSRF. The ROE for the CWSRF fluctuates slightly from year to year as shown below. The ROE rate is adequate considering WVDEP's CWSRF program generally offers loans to its borrowers with interest rates averaging less than one percent and interest rates on invested funds are near zero percent for the liquidity accounts. Although ROE decreased slightly from 2016, it has been increasing over the last



four years. The four-year average is 0.95%:

2014 – 0.54%  
2015 – 0.96%  
2016 – 1.20%  
2017 – 1.08%

WVDEP periodically performs long-term cash flow modeling and long-term planning of the CWSRF. Modeling estimates the availability of cash flows to fund projects over the next several years. Cash Modeling is an estimate of the financial capacity of the CWSRF over time. It provides decision makers with the amount of funding available over three to five years. As needed, modeling can provide longer term projections to inform CWSRF program managers considering potential changes to loan terms.

EPA concludes that WVDEP continues to manage the CWSRF program in a manner that ensures the Fund will be available in perpetuity as a permanent source of financing of water quality infrastructure facilities. This conclusion is based upon a review of the audited financial statements, annual report, the financial management policies and procedures, and the following:

- The CWSRF fund account has a strong cash flow;
- Financial management is sound;
- Internal controls are in place;
- Annual independent audits are performed;
- All funds are invested prudently;
- The Public Service Commission performs detailed initial credit analysis and financial capability assessments on all municipal borrowers;
- WVDEP provides strong loan monitoring of borrowers during construction and repayment periods;
- State match is deposited in one lump sum when EPA grants are awarded; and
- There is no debt.

### **New Financial Indicators**

To address a high priority recommendation from the Government Accountability Office's (GAO) August 2015 report, three new financial indicators were developed in collaboration with state and EPA SRF managers. During next year's annual review, these three new indicators will be reviewed in addition to the financial indicators currently reported in CWSRF National Information Management System (CWNIMS). The purpose and value of these new indicators were discussed with WVDEP staff.

Beginning with SFY 2018 data, EPA will analyze the new indicators, comparing the most recent three years of data, as part of the annual review. The data to calculate the indicators is pulled directly from CWNIMS. The new financial indicators and how they are calculated is included below.

- Ratio of Undisbursed Project Funds to Disbursements – key component of SRF fund management is the balancing of cash inflows and outflows. This ratio evaluates how efficiently SRF funds are revolving by examining the program's disbursement rate over a set

period of time and comparing it to the amount of cash on hand. This indicator should either remain stable or decrease over time

- Undisbursed Project Funds / 3 Year Average Annual Disbursements
- Total Net – measures the extent to which internal growth generates additional funding for new projects. This is accomplished by taking total cash inflows generated by ongoing loans and investments and subtracting out the total outflows resulting from leveraging activity. This indicator should either remain stable or increase over time.
  - $(\text{Loan Interest} + \text{Investment Interest} - \text{Bond Interest}) - (\text{Match Bond Principal} + \text{Loan Principal} - \text{Leveraged Bond Principal})$
- Net Interest Margin – measures the net earnings the SRF generates from its Total Assets through loans and investments after accounting for the interest expense associated with match and leveraged bonds. This indicator does not include Match Bond principle payments as an expense like the existing Retained Earnings metric. This indicator should either remain stable or increase over time.
  - $\text{Net Interest} / (\text{Total Assets Prior Year} + \text{Total Assets Current Year}) / 2 * 100$

### **Audits of the Fund**

On October 10, 2017, the State's independent certified public accountants (CPAs) issued the West Virginia CWSRF audited financial statements. The audit included an unmodified opinion on the financial statements, indicating that they were fairly stated in accordance with generally accepted accounting principles (GAAP). There were no findings or recommendations in the audit report.

The WVDEP CWSRF (CFDA No. 66.458) financial audit report includes the Single Audit. There were no findings or questioned costs. The amount reported in the Schedule of Expenditures of Federal Awards equaled the amount reported to EPA on WVDEP's Federal Financial Reports, totaling \$20,829,000.

### **Prior Year Action Items**

There were no action items for WVDEP as a result of the FY 2016 annual review.

We appreciate you and your staff's continued cooperation and support without which, it would be impossible for us to complete the statutorily required annual review timely. Should you have any questions, please contact Kimberly Scharl at 215-814-5428 or me at 215-814-5435.

Sincerely,



Lorraine H. Reynolds, Associate Director  
Office of Infrastructure and Assistance

cc: Katheryn Emery, WVDEP